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AIR UNIVERSITY

THE NORTH AMERICAN FREE TRADE AGREEMENT
LOPSIDED POTENTIAL, LOPSIDED PROBLEMS

by

Thomas C. Lorimer, Lt Col, USAF

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Advisor: Dr. James Winkates

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Air War College
Maxwell AFB, Al 36112

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Abstract

The North American Free Trade Agreement (NAFTA), which was signed on August 12, 1992, links the economies of the United States, Canada, and Mexico, creating an \$8 trillion, 380-million person market, the world's largest. This paper reviews the effects of NAFTA on the three economies involved, covers the basic terms of the agreement, and looks at the results (economic and political) of the pact. The particular emphasis of the paper is on Mexico. The economy of Canada is already closely linked with that of the United States due to cultural, economic and legal similarities. Mexico, however, represents a potential threat to American security interests. Exploding populations, illegal immigration, chronic poverty, political instability, and the possibility of civil unrest, make Mexico an uncertain friend south of the border. The paper concludes that only a prosperous Mexico is not a threat to U.S. national security, and NAFTA is the best available mechanism to bring that about.

Chapter 1

Introduction

The four traditional “pillars” of national security are the economy, the military, politics, and culture. Working backwards from the above list, nations with “desirable” or admired cultures are ascribed higher levels of national security because that desirability influences other nations to curry favor, or at least not threaten, the object of their admiration. Politics refers to the ability of a nation to enforce its will on other nations or groups by non-military means, such as diplomacy, persuasion, unexecuted threats or promised rewards. In the Clausewitzian world, politics (or diplomacy, to use his term) is the cheaper, neater precursor to the second pillar of national security, the military. The importance of military forces is obvious, because vital national interests are often only able to be resolved by force. It is sometimes easy—particularly at institutions such as The Air War College—to concentrate only on the political and military aspects of national security; that is, upon the precursor to war, and war itself. This is natural, since most of the students and faculty are or have been in the military, and their interests, experiences and training have been in preparing to fight and fighting itself. This pre-occupation with the military and political pillars sometimes obstructs our view of the first pillar, the economic basis of national security.

But the implications of the state of a nation's economy upon its national security can be enormous. After all, it is the economy—the underlying wealth and productivity of the nation—that pays for the military forces, training, and equipment. As 20th century events have proven, however, a balance of strengths is essential for continued national security. Great Britain, victorious but economically drained in two costly world wars, was unable to pay for the military forces needed to defend its empire, which it subsequently lost. The Soviet Union was unquestionably a military superpower, but it disintegrated because it was *only* a military superpower, not an economic one as well. This lopsided-ness can cut the other direction, too—Japan and Germany, although economic superpowers and potential members of the United Nations Security Council, lack appropriate balance among the three main pillars of national security and are virtually unable to defend themselves.

As the United States sorts out its role as the remaining superpower in the post cold war world, it is important to consider what we can (and are doing) to improve the economic basis of our national security. Patterns of national competition are shifting—in the cold war, military strength was paramount, political influence was next in importance, and the economy was frequently taken as a given. The United States was fortunate in that we emerged from World War II wealthy, undamaged and *the* predominate economic power on earth. We could therefore afford to wage—meaning pay for—the Cold War. We could make a choice about our national defense. Now, new threats are emerging to our economic well-being, which in turn threaten our ability to choose the force structures we may feel are necessary. New competition, a sort of global “gold rush,” has broken out among trading blocks in Europe, Asia, and North America for markets, resources, and

economic advantage. If the United States loses the trade war, will it be *able* to afford the military forces it needs? And, if the United States becomes isolated and protectionist, what are the consequences to our national security?

This paper examines one track—the North American Free Trade Agreement or NAFTA—the United States has taken to compete in the global trading bloc wars. This paper examines the NAFTA agreement, its provisions, side agreements, advantages and disadvantages, and then assesses its impact upon the economic and non-economic aspects of our national security.

Chapter 2

The North American Free Trade Agreement

The North American Free Trade Agreement (NAFTA), which was signed on August 12, 1992, links the economies of the United States, Canada, and Mexico, creating an \$8 trillion, 380-million person market, the world's largest.¹ Its stated goal is to "... eliminate barriers in trade... promote conditions of fair competition... [and]... increase substantially investment opportunities."² This agreement, signed by President George Bush and approved by Congress early in the administration of President Bill Clinton, was the culmination of a long and difficult series of negotiations among the U.S., Canada, and Mexico. The idea for a North American free-trade zone originated with President Ronald Reagan. The pact took effect on January 1, 1994, with full and final implementation scheduled for January 1, 2008. As will be discussed later, NAFTA has some important non-economic implications for the three nations involved and has been subject to severe criticism from many sectors of the American public.

Notes

¹"Fact Sheets: Canada." *U.S. Department of State Dispatch*, Vol. 6, No. 10, March 6, 1995, p. 166.

²*The NAFTA, Volume I*. Washington, DC, U.S. Government Printing Office, 1993, Preamble.

Chapter 3

Prior Trade and Investment Patterns: U.S. And Canada

Canada is the United States' largest trading partner, and the economies of the these two countries are deeply intertwined. As President Clinton noted, "[o]urs [i.e., the U.S./Canadian relationship] is the world's most remarkable relationship whether we like it or not."¹ As Table 1 demonstrates, trade and investment between the U.S. and Canada is extensive:

Table 1. Trade and Investment Patterns: U.S. and Canada

Billions, U.S.	1991	1992	1993	1994
U.S. Merchandise Exports to Canada	85.1	90.6	100.2	114.8
U.S. Merchandise Imports from Canada	91.1	98.5	111.2	131.1
U.S. Direct Investment in Canada	75.5	73.2	73.3	70.6
Canadian Direct Investment in the U.S.	51.0	50.9	50.5	49.8

Source: "Business Fact Sheet: Canada." U.S. Department of Commerce, NAFTA Facts Canada, [(202) 482-4464], Document #7101, October 13, 1995, p. 2.

The main U.S. exports to Canada are autos, trucks, auto parts, engines, cathode tubes, computers, and electrical machinery.² Canada exports cars, trucks, and automotive parts, wood and paper products, aluminum, oil and natural gas, and computer parts to the U.S.³ Eighty-four percent of Canada's exports are sent to the United States.⁴ Altogether, 4.5 million American jobs are connected, either directly or indirectly, with U.S./Canadian trade.⁵

Two prior trade agreements significantly affect U.S./Canadian trade relationships. The 1965 Auto Pact allowed for duty-free trade for most automobiles and automotive parts between the two countries.⁶ As a result, Canadian manufacture of cars and trucks accounts for 10% of the North American market.⁷ In 1994, Chrysler alone produced 695,000 vehicles in Canada.⁸ This pact explains the high flow of automotive-related items across our northern border. The U.S.-Canada Free Trade Agreement of 1989 opened up other areas of trade, notably trade in services and free flow of most investments.⁹ This pact, with some modifications and the addition of certain side agreements, later became the basis of NAFTA. It has been noted that because of the prior success of these two pacts and the legal, cultural and economic similarities between the two nations, NAFTA barely had an impact on U.S./Canada trade.¹⁰ Canada, however, could “. . . not afford to stay out of the continental trade agreement [i.e., NAFTA] for fear of losing the benefits of its earlier trade agreement with the United States and being out-competed by Mexico in American markets.”¹¹ These two facts—the minimal impact of NAFTA on U.S./Canadian relations and Canada’s fear of being odd-man out—suggest two important points about NAFTA. First, whatever trading changes that have occurred under NAFTA with regard to Canada would probably have happened anyway, because most of the mechanisms for free trade were already in place. And second, the North American Free Trade Agreement—its potential, its many problems, and the criticisms of it—has very little to do with Canada. After all, Canada, even a Canada fragmented into English and French speaking parts, is not a threat to the United States. NAFTA is really about Mexico.

Notes

¹"The United States and Canada: Reaffirming the Partnership." Remarks by President Bill Clinton. *U.S. Department of State Dispatch*, Vol. 6, No. 10, March 6, 1995, p. 161.

²"Business Fact Sheet: Canada." U.S. Department of Commerce, NAFTA Facts Canada, [(202) 482-4464], Document #7101, October 13, 1995, p. 2.

³Ibid.

⁴"Fact Sheets: Canada." *U.S. Department of State Dispatch*, Vol. 6, No. 10, March 6, 1995, p. 165.

⁵"The United States and Canada: Reaffirming the Partnership." Remarks by President Bill Clinton to the Canadian Parliament, Ottawa, Canada, February 23, 1995. *U.S. Department of State Dispatch*, Vol. 6, No. 10, p. 164.

⁶"Fact Sheets: Canada." *U.S. Department of State Dispatch*, Vol. 6, No. 10, March 6, 1995, p. 165.

⁷AL, Symonds, William C. "Meanwhile, To The North, NAFTA Is A Smash." *Business Week*, February 27, 1995, p. 66.

⁸Symonds, William C. "Meanwhile, To The North, NAFTA Is A Smash." *Business Week*, February 27, 1995, p. 66.

⁹"Fact Sheets: Canada." *U.S. Department of State Dispatch*, Vol. 6, No. 10, March 6, 1995, p. 165.

¹⁰Davis, Bob. "Two Years Later, the Promises Used to Sell NAFTA Haven't Come True, but Its Foes Were Wrong, Too." *The Wall Street Journal*, October 26, 1995, p. A24.

¹¹Fox, Annette Baker. "Environment and Trade: The NAFTA Case." *Political Science Quarterly*, Vol. 110, No 1, 1995, p. 51.

Chapter 4

Prior Trade and Investment Patterns: U. S. and Mexico

Mexico is very different from either the United States or Canada. The Mexican economy is small (approximately 1/30th the size of the United States¹) and, relative to Canada, protected by tariffs averaging 10% (compared with 4% for Mexican goods entering the United States).² In effect, prior to NAFTA, the United States economy was wide open to Mexico, and the Mexican economy was closed to the United States.³ Trade and investment patterns are shown in Table 2.

Table 2. Trade and Investment Patterns: U.S. and Mexico

Billions, U.S.	1991	1992	1993	1994
U.S. Merchandise Exports to Mexico	33.3	40.6	41.6	50.8
U.S. Merchandise Imports from Mexico	31.2	35.2	40.0	49.5
U.S. Direct Investment in Mexico	35.9	37.5	42.4	49.5
Mexican Direct Investment in the U.S.	N/A	N/A	N/A	N/A

Source: "Business Fact Sheet: Mexico." U.S. Department of Commerce, NAFTA Facts, Document #8101, [(202) 482-4464], September 19, 1995, pp. 2-3.

Principal U.S. exports to Mexico include autos and automotive parts, franchises, apparel, aircraft and electronics parts, and pollution, chemical, and communications equipment.⁴ The automotive sector of U.S. exports to Mexico could be particularly important—the Commerce Department suggests that the Mexican automobile market is the only one in the western hemisphere that is expected to grow in the 90s decade.⁵ Principle U.S.

imports from Mexico include assembled computers, iron and steel, oil, and a variety of agricultural products.⁶

Two prior agreements have affected U.S./Mexican trade relations. The "Bracero" program permitted Mexicans easy access to U.S. labor markets prior to 1965. The program was terminated because temporary workers often (illegally) became permanent but undocumented residents. The Bracero program was replaced by the "*maquiladora*" system (translation: "assembly plant"), a free-trade zone that stretches along the U.S.-Mexican border from California to Texas.⁷ Four hundred thousand workers⁸ are employed at approximately 2,000, mostly jointly owned plants, earning Mexico \$3.5 billion in foreign currency each year (an amount second only to Mexico's earnings from exporting oil).⁹ Typically, unfinished goods or unassembled components from U.S. firms are finished and assembled in the *maquiladoras* for re-shipment to the U.S. or for export to other nations.¹⁰ In effect, the 20-mile wide *maquiladora* corridor is a mini, Mexican-only NAFTA which exploits one of Mexico's few economic advantages—cheap labor. The *maquiladora* system provides American manufacturers with an effective way to stay in business in the face of stiff competition from Asia.¹¹

Mexico is also a nation undergoing a difficult transition. It has a low standard of living (\$3,600 per capita gross domestic product¹²), a rapidly growing population (92 million in 1994, which is expected to grow to 136 million in 2020¹³), an immature economic infrastructure and a political system which has recently been wracked by upheaval, corruption, and near civil war. Mexico has been called a third-world country "... set to join the first world."¹⁴ Prior to implementation of NAFTA, the Mexican economy was dominated by government investment and ownership, over-regulation, and

high tariffs (averaging 10% on U.S. goods¹⁵), and was generally insulated from outside competition and investment. NAFTA has been called a “mutually advantageous cooperation between developed and developing countries.”¹⁶ Along with other economic and political adjustments made by the Mexican government, NAFTA is seen as an essential step in Mexico’s quest to leave the third world behind.

Notes

¹Roberts, Steven V., with Impoco, Jim. “The new trade tussle.” *U.S. News & World Report*, April 15, 1991, p. 45.

²Rutledge, John. “Economic Outlook: Free Trade With Mexico Will Boost America’s Economy.” *U.S. News & World Report*, May 13, 1991, p. 58.

³Dornbusch, Rudiger. “North American Free Trade: What It Means.” *The Columbia Journal of Business*, Summer 1991, p. 73.

⁴“Business Fact Sheet: Mexico.” U.S. Department of Commerce, NAFTA Facts, Document #8101, [(202) 482-4464], September 19, 1995, pp. 2.

⁵“Key NAFTA Sector-Specific Provisions.” U.S. Department of Commerce, NAFTA Facts, Document #3001, [(202) 482-4464], September 12, 1994, p. 1.

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⁷Whiting, Van R., Jr. “Policy Choice and Global Structure.” *The Columbia Journal of World Business*, Summer 1991, p. 141.

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⁹*Ibid.*, p. 43.

¹⁰Fox, Annette Baker. “Environment and Trade: The NAFTA Case.” *Political Science Quarterly*, Vol. 110, No 1, 1995, p. 53.

¹¹Dornbusch, Rudiger. “North American Free Trade: What It Means.” *The Columbia Journal of Business*, Summer 1991, p. 79.

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¹³*Ibid.*, no page cite.

¹⁴Kay, Roger L. “Making the Mexico Connection: One Year After NAFTA.” *Computerworld*, December 19, 1994, p. 36.

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¹⁶Bello, Judith F. and Holmer, Alan F. “The North American Free Trade Agreement: Its Major Economic Benefits, and Overarching Implications.” In, *The North American Free Trade Agreement: A New Frontier in International Trade and Investment in the Americas*, Bello, Judith H. and Holmer, Alan F., Editors. Washington, DC, The American Bar Association, 1994, p. 10.

Chapter 5

Synopsis of NAFTA's Provisions

NAFTA, in stages, will eliminate all U.S./Canadian/Mexican tariffs by the year 2008, starting with an immediate 50% reduction on industrial tariffs, followed by a complete elimination of industrial tariffs by 2004, and a gradual elimination of agricultural tariffs.¹ These tariffs apply only to goods made in North America, not to goods imported from or, re-imported into, other countries.² Tariffs aside, NAFTA also provides for simplification of trade: that is, standardization and reduction of customs applications and rules,³ and elimination of so-called "standards barriers (i.e., artificial standards unrelated to product performance or suitability which effectively act as a tariff). The agreement includes important provisions allowing repatriation of profits and capital (a frequent concern facing investors contemplating doing business in under-developed countries)⁴ and "... the best intellectual property provisions ever negotiated by the United States. . . ."⁵ This provision is particularly important on the Mexican side of the agreement, where the latest software is routinely pirated and, according to the Motion Picture Association, 50-60% of the pre-recorded video tapes sold are bootlegged.⁶ NAFTA eases travel restrictions for professional persons and the "tools of their trade."⁷ It also simplifies cross-border transportation—seventy-five percent of American trade with Mexico moves by truck, which, under the provisions of the agreement, will be permitted access to highways in the

border states of each nation.⁸ NAFTA members will have greater, but not unlimited, access to each other's government procurement sectors (a \$90 billion market⁹) and to the member nation's services industry. This provision is particularly important to the United States, which commands 19% of the global services market and runs large "services" trade surpluses with both Canada and Mexico, our second and fifth largest services customers.¹⁰ NAFTA contains "content rules" to prevent so-called "touch-and-go" importation from a non-NAFTA country solely for the purpose of taking advantage of low tariffs.¹¹ The pact also includes mechanisms for settling trade disputes. NAFTA may be terminated upon six months notice by any one of the three parties.¹²

Beyond describing what NAFTA *is*, it is also important to understand what NAFTA is not. It is not a "common market" (i.e., a borderless economy) along the lines of the European Union.¹³ Nor is it a global "free trade" agreement—it is an American, Canadian, and Mexican free trade pact, *to the exclusion of other nations*. It does not exempt Canadians or Mexicans conducting business in the United States from complying with applicable professional licensing and certification requirements,¹⁴ nor does it permit foreign cargo carriers to operate in the United States without complying with domestic safety standards. In addition, NAFTA does not open all markets to no-holds-barred competition. The Mexican oil industry, for example, is excluded because of its special status under the Mexican Constitution.¹⁵ Similarly, Canada fears that its "uniqueness" is being overwhelmed by American popular culture and has retained formal import restrictions on U.S. media into their country.¹⁶ There are even provisions to protect unique national products—for example, Kentucky Bourbon, Canadian Whiskey, and Mexican Tequila—from competition. NAFTA also protects U.S. industries from

immediate and damaging competition from Mexican or Canadian producers. "Surge" provisions have been incorporated to allow tariffs to "snap back" to the prevailing levels before NAFTA for three or four years (depending on the product), if there is evidence that the new pact results in harm to U.S. workers or firms.¹⁷

The NAFTA treaty received strong support from the six American presidents living at the time of implementation, endorsement by seventeen American Nobel Economics laureates,¹⁸ and the approval of seventy percent of the nation's top businessmen and women.¹⁹

Notes

¹"Key NAFTA Sector-Specific Provisions." U.S. Department of Commerce, NAFTA Facts, [(202) 482-4462], Document #3001, September 12, 1994, p. 1.

²*Ibid.*, p. 2.

³"Fact Sheets: Canada." *U.S. Department of State Dispatch*, Vol. 6, No. 10, March 6, 1995, p. 166.

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⁶"Mexico To Cut Piracy." *Reuters/Variety*, November 9, 1995, no page cite, *via America Online*.

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¹¹"No social contract." *The Economist*, February 18, 1995, p. 24.

¹²Bello, Judith F. and Holmer, Alan F. "The North American Free Trade Agreement: Its Major Economic Benefits, and Overarching Implications." In, *The North American Free Trade Agreement: A New Frontier in International Trade and Investment in the*

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¹⁶*Ibid.*, p. 87.

¹⁷"Key NAFTA Sector-Specific Provisions." *U.S. Department of Commerce*, NAFTA Facts, Document #3001, [(202) 482-4464], September 12, 1994, p. 3.

¹⁸Tobias, Andrew. "Money Angles: Why NAFTA Is Good Medicine." *Time*, November 12, 1993, no page cite, *via America Online*.

¹⁹"Business Briefs—December 1, 1995." Community Television Foundation of South Florida, Inc., no page cite, *via the Internet*.

Chapter 6

Synopsis of NAFTA's Side Pacts

From its inception, the NAFTA pact has been dogged by criticism. The agreement was negotiated under so-called “fast-track” authority granted by Congress. The fast track authorized the executive branch to reach an agreement with Canada and Mexico upon which the Congress would then vote “up-or-down:” that is, no change to the pact could be inserted during congressional debate. This provision was necessary to give negotiators credibility with their foreign counterparts. After all, no one would agree to a trade pact if they did not know what the final product was actually going to be. However, to get “fast-track” authority, President Bush agreed to monitor three areas which were causing significant levels of political concern—displacement of U.S. workers, health and safety programs for the Mexican workforce, and environmental standards, particularly along the Mexican border.¹ Side pacts were negotiated to monitor the status of these issues.

To address anticipated U.S. job losses, the Department of Labor has established a program (the Transitional Adjustment Assistance program) to provide job re-training for those who have been “certified” as losing their jobs because of NAFTA.² The program was created to provide retraining, college assistance and even moving expenses for those who lose their jobs because of the NAFTA agreement. The Transitional Adjustment

Assistance program receives \$66 million in yearly funding, and is designed to assist up to 150,000 people.³

For the Mexican health and safety issues, the Commission on Labor Cooperation was established to promote uniform “. . . laws, standards, application and enforcement . . .” in the work place.⁴ Its headquarters is in Dallas, Texas and is led by a Canadian.⁵

Two separate commissions were created to monitor the environment: The Commission on Environmental Cooperation in Montreal deals mainly with U.S./Canadian ecological issues. The Border Environmental Cooperation Commission, located in Juarez, Mexico, and headed by a Mexican, deals with the more difficult problem of U.S./Mexican cross-border pollution, which is potentially hazardous to both U.S. and Mexican citizens alike.⁶ While there has been some dispute about the effectiveness or even practicality of these organizations—one critic labeled them “. . . a bit of a fraud, sweeteners . . . added to win reluctant [congressional] votes, . . .”⁷ NAFTA and its side pacts are unique because they directly link international trade with social policies and goals.⁸

Notes

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³Ibid.

⁴“Fact Sheets: Canada.” *U.S. Department of State Dispatch*, Vol. 6, No. 10, March 6, 1995, p. 168.

⁵“No social contract.” *The Economist*, February 18, 1995, p. 24.

⁶Ibid.

⁷“NAFTAmath.” *The Nation*, January 2, 1995, p. 4.

⁸“No social contract.” *The Economist*, February 18, 1995, p. 24.

Chapter 7

Implied Objectives of NAFTA

NAFTA is more than just a trade pact. Beneath the complex and lengthy language of the agreement are several unstated but nevertheless important agendas, almost exclusively having to do with Mexico. The first and most obvious of these subtexts is illegal immigration. According to Ambassador Julius Katz, Deputy United States Trade Representative, migration, illegal or otherwise, was “. . . not considered to be a subject of the [NAFTA] negotiations.”¹ In saying this, Ambassador Katz was technically correct—NAFTA did not establish a free labor pool, such as was created by the European Union.² Wealthy nations, which can afford to make choices about their national defense, often look at other similarly equipped nations as potential adversaries. Conversely, poor nations, which cannot support large military force structures, are frequently *overlooked* as potential threats. But poor nations (of which Mexico is a prime example) have peculiar powers in that poverty and political instability create refugees and illegal immigrants. Once these economic refugees arrive in the destination country of their choice (in this case, the United States), they are difficult and expensive to apprehend, detain, and repatriate. In addition, the fact that illegal immigration is occurring stimulates domestic discontent and results in intense political pressure to “do something” about the problem. Our experiences with Haitian and Cuban refugees, who crossed open seas to reach the

United States, demonstrate how powerless the United States is in preventing illegal migration. The 2,000-mile U.S./Mexican border, where a very rich nation and a very poor one meet, is easier to cross than open water, and the number of potential Mexican immigrants is many times larger than either Haiti or Cuba could generate. Employment opportunities and American culture are attractive to poor Mexicans, particularly when amplified by the dominate U.S. media. In modern times, however, only the Berlin Wall has been an effective deterrent to unauthorized immigration. The United States, then, has a serious and perhaps un-solvable security problem on its southern border. The NAFTA pact was a back door attempt to control this potentially huge exodus of refugees across our 2,000-mile border with Mexico. Creating jobs and prosperity in Mexico was viewed as one of the few practical ways to keep Mexicans at home.

Another unstated objective for the United States was access to energy sources. Barring the unlikely event of another major oil discovery in the United States, domestic oil reserves will continue to fall and imports will grow. The Arab oil boycotts of the 1970s and the 1991 Gulf War prove that Middle Eastern supplies are in politically unstable regions and vulnerable to disruption. Our NAFTA partners to the north and south, however, have significant, exportable reserves. Combined, North American oil reserves account for 8% of the world's total, and two-thirds of that is in Mexico.³ Over 60% of Mexican oil exports go to the U.S.⁴ Canada and Mexico together are the third and fourth largest sources of imported U.S. oil, 24% of total U.S. imports.⁵ NAFTA effectively gives the United States *preferred access* to these energy sources. Mexico also has significant reserves of natural gas. (As an interesting sidelight, NAFTA may also be a bonanza for American producers of energy-related equipment—according to one estimate, Mexico will

need to spend between \$20 and \$30 billion before the turn of the century in order to modernize its oil facilities.⁶⁾

NAFTA is also a counterbalance to other international trading blocs and regions. The European Union is rapidly becoming a major force in international trade, as is the Association of South-East Asian Nations. Trading pacts are also springing up in South America, as with the 1988 Mercosur agreement between Brazil, Argentina, Uruguay, and Paraguay. These trade pacts have recognized the generally held belief that economic growth is not possible without becoming export-oriented.⁷ Larger, tariff-free markets also allow manufacturers to gain further advantage from their existing economies of scale. This "gold rush" of forming trading and export blocs may be the new form of international struggle, perhaps replacing military force structure as the primary arena of competition. "The architecture of the new world trading system might be one where NAFTA members and the European Union create blocks that fight each other with massive tariff barriers."⁸ The process of including some other nations in your trading bloc is also an *exclusion* of the remaining others from the advantages that bloc may offer. In the particular case of Mexico and Canada under NAFTA, we transform potential trading opponents into allies, putting them effectively "off limits" to other competitors, and increasing our influence over them.⁹

Notes

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Chapter 8

Objections to the NAFTA Agreement

Since its inception, critics have bitterly opposed the NAFTA treaty, citing both economic and non-economic reasons. These objections are principally about the conditions in Mexico and the potentially adverse effects Mexico may inflict on the United States under the terms of the treaty.

Employment Losses

Perhaps the most widely expressed fear is the concern about losing American jobs to the lower-paid Mexican force. Ross Perot, one of the most notable NAFTA foes, charges that 5.9 million jobs are at risk from the “giant sucking sound” south of the border.¹ (Interestingly enough, White House polls found that public support for NAFTA increased if those who were being polled were aware that Ross Perot was against it.²) The AFL-CIO predicts 500,000 losses by the year 2000.³ The Amalgamated Textile Workers Union forecasts one-half million job losses from its members alone.⁴ There is wide-spread fear that industries, particularly low-skill industries, will engage in what Supreme Court Justice Louis Brandies called “the race to the bottom:”⁵ that is, a relentless pursuit of the cheapest labor, wherever it is located. The controversy has even taken on a gender slant—many American textile workers are women, leading to charges that “[b]ig business

will . . . pit working women in industrialized countries against much lower paid women in 'developing countries'."⁶ It is certainly true that Mexican workers earn less than an American would employed at a similar task. It is important to remember, though, that low Mexican wages are reflective not only of different standards of living, but also low Mexican productivity.⁷ Mexican autoworkers, for example, make about \$6 per hour, far less than their Detroit counterparts, but because of limited automation, their productivity is also lower.⁸ In low-skill industries, some Mexicans earn \$1 per hour, or less.⁹ One supporter of NAFTA, commenting on competition from low-paid foreign workers, noted that if poverty were an unfair competitive advantage, ". . . Bangladesh would be an even more formidable competitor [than Mexico]."¹⁰ Critics of the NAFTA accord (including Ross Perot) have proposed a "social tariff," which would assess duties on imported Mexican goods at a level sufficient to equalize the difference between the wage rates in the two countries.¹¹ In addition, the controversy over "jobs lost" reflects a long-festering uneasiness in the American labor pool. The effects of automation have had negative effects on the low-skill end of the work force. By one estimate, 100 to 150 workers can produce today what it took 300-400 to produce just 15 years ago.¹² As a result, many corporations are "downsizing," and those of the newly unemployed who have weak job skills may become permanently unemployed or be unable to find comparable work.¹³ According to the Congressional Office of Technology Assessment, "[d]isplaced manufacturing workers frequently suffer substantial wage cuts. The future seems especially grim for workers with modest levels of education attainment and skill."¹⁴

Although there probably have been some jobs lost, the most exaggerated fears of American workers have not been realized. The Department of Labor has provided

NAFTA-certified job loss training to about 50,000 workers.¹⁵ This figure does not include job *gains* attributed to NAFTA, which are more difficult to survey and often depend on one's political viewpoint. President Clinton claims 200,000 new NAFTA jobs in the first two years of the agreement.¹⁶ Another survey, conducted by the Joint Economic Committee of the House of Representatives, concluded that the net job effect was a loss of 10,000.¹⁷ *The Wall Street Journal* estimates no net job increase yet, but attributes that primarily to the collapse of the Mexican economy.¹⁸ Complicating the job accounting is the fact that while the American economy loses about two million jobs every year, the net job growth is two million jobs per year.¹⁹ This churning and rate of growth makes most of the losses attributed to NAFTA seem small by comparison.²⁰

Affected Industries

The NAFTA literature uses the unfortunate terms “winners” and “losers” for those industries which will benefit from the agreement or be harmed by it. While the win/lose terminology carries some emotional baggage with it, the labels do reflect an obvious fact—some will benefit, but others will be hurt. Complete understanding of the jobs lost or created by NAFTA requires an examination of which industries will be most affected. Those employed in making high-quality or high-technology products—metal alloys, capital goods, machinery, textiles (i.e., woven cloth), automotive parts, communications and computer products—will benefit from free trade with Mexico.²¹ Services, such as banking and franchising, some sectors of the agricultural economy (grains, meats and some produce),²² and producers of consumer goods (beverages and cosmetics)²³ will also be “winners.”²⁴ (The rapid influx of American service businesses—McDonald's, Wal-

Mart, etc.—has some Mexicans joking that NAFTA stands for North American *Franchise* Trade Agreement.²⁵) The pact has created a boom north of the Mexican border in shipping and trucking centers such as Laredo, Texas²⁶ and (until the Mexican recession hit), an explosion of auto exports to Mexico (up 500% in 1994 alone).²⁷ Ford particularly has benefited, increasing its Mexican market share from 14.2% in September 1994 to 18.6% a year later.²⁸

At-risk industries include apparel (i.e., ready-to-wear garments), shoes, established “rust belt” type of industries,²⁹ parts of the agricultural sector (e.g., citrus and some types of produce), and furniture.³⁰ The obvious conclusion from this list of NAFTA winners and losers is that American workers are no longer competitive in low-skill, low-tech jobs. The president of a knitting mill which was moving its operations to Mexico correctly assessed the situation: “. . . all our labor-intensive manufacturing in the United States will dissipate to nothing by the year 2000 or so.”³¹ If this prediction becomes true, it would only be the culmination of a decades-long flight of such industries to cheaper labor markets in other parts of the world.³² A final and telling feature of the losing side (clothing, shoes, basic steel, agriculture) is that these are sectors already highly protected by tariffs and, in some cases, even subsidized, a clear indication of un-competitiveness.³³

Looking at the other side of the list—the NAFTA winners—demonstrates several important points as well—high-tech jobs require skills that will not easily be found in Mexico, providing an obvious incentive for these firms to stay north of the border. In addition, finding the cheapest wage rates is not the only strategy a business can use to remain competitive. Automation offers high-tech industries another way to improve productivity.³⁴ Finally, the infrastructure advantages of the United States as well as its

familiar legal system and stable government, offer additional incentives to remain located “domestically.”³⁵

The Environment

Nearly as intense as the objections to jobs lost and industries damaged are environmental concerns about NAFTA. Pollution in Mexico is extensive (the country of Mexico is sometimes referred to as a “pollution haven”) and it poses a threat not only to Mexicans, but also to Americans living north of the border. The Rio Grande River has been called “a 2,000-mile Love Canal,” referring to the notoriously toxic and now off-limits neighborhood in Niagara Falls, New York.³⁶ Raw sewage from Tijuana, Mexico flows into the Pacific Ocean and drifts northward past San Diego and Los Angeles.³⁷ Coal-fired power plants in Mexico cloud the skies over Big Bend National Park in Texas.³⁸ The ground water in Nogales, Arizona is contaminated with cancer-causing chemicals dumped by the *maquiladoras* across the border.³⁹ Anti-NAFTA environmentalists argue that accelerating the industrial development of Mexico, especially in the *maquiladoras* border zone, will only worsen the pollution in the area. In addition, they charge that since Mexican environmental laws are not as strict as those north of the border, not having to comply with “American” anti-pollution requirements is, in effect, an “environmental subsidy” for Mexican products.⁴⁰

While NAFTA’s side agreements obligate Mexico to make environmental changes, progress in this area has been very slow. On the surface, Mexico’s 1988 environmental laws appear to be adequate—in fact, these provisions were closely patterned on United States environmental statutes.⁴¹ Despite a few notable exceptions (including the

temporary shutdown of one of Pemex's [the Mexican national oil company] main refineries), they are rarely enforced. Part of the problem is resourcing—Mexico spends 48 cents per person per year on environmental programs (the U.S. spends \$24.40) and has only 12 inspectors working in the entire *maquiladoras* zone.⁴² In addition, inspectors have a large amount of “discretion” in enforcing Mexican environmental law, leading some to suspect corruption and bribery are widespread.⁴³ Smaller manufacturers in the *maquiladoras* zone could even be forced out business by strict enforcement of existing environmental laws.⁴⁴ Finally, the North American Development Bank, which was set up by NAFTA to finance environmental cleanup along the border had not, as of September 1995, made any loans for that purpose.⁴⁵ Nevertheless, there has been some progress made—the United States Filter Corporation has landed several large contracts to build waste water treatment plants in Mexico. The environment, however, remains a “wait-and-see” type problem—perhaps, in the future, NAFTA will help create a more prosperous Mexico which will more interested in and better able to take care of their environment.⁴⁶ In the absence of prosperity, however, continued environmental degradation along the border will certainly continue.

Health and Safety

Health and safety issues are another source of NAFTA criticism. As with their environmental regulations, Mexican occupational health and safety practices *on paper* substantially resemble those in the United States.⁴⁷ The reality, however, is much different. Mexican industries use joint labor/management committees to review and enforce worker safety laws. Often, however, these committees are creatures of manage-

ment and subject to manipulation and top-down coercion.⁴⁸ Information about workplace hazards and the protective equipment and training needed to create a safe job environment are in short supply or non-existent.⁴⁹ Committee members who express too much concern about these issues may be subject to dismissal. Child labor laws are also different in Mexico, where the minimum working age is 14 (with limited working hours). At age 16, however, no hourly limit applies.⁵⁰ Although Mexico is also more highly unionized than is the United States,⁵¹ the unions are “supervised” by the government⁵² and considered to be ineffective in negotiating better working conditions. This disparity in working conditions, coupled with the potential loss of jobs in the U.S., gives NAFTA critics a powerful one-two punch: “You lost your high paying job to NAFTA, and your former employer took that job and sent it to a sweat shop in Mexico.”

Safety critics are not concerned just about Mexican safety, but also about safety on the American side of the border. As mentioned earlier, the NAFTA pact permits Mexican truckers to deliver goods in the states along the border. (Prior to NAFTA, they could deliver within 20 miles of the border.) The same is true for American trucking firms in Mexican border states. There are serious concerns about the safety of Mexican trucks—for example, Mexican trucks are not required to have front brakes, the rigs are frequently in poor repair,⁵³ and drivers are not trained to handle hazardous cargo.⁵⁴ In addition, there are no maximum hours which can be legally driven in a 24-hour period.⁵⁵ Inspection is also spotty—approximately 4,000 trucks cross the border at Laredo, Texas, each day, but the customs station has only 20 agents available to make safety checks. Fifty-two percent of Mexican trucks inspected at the border fail, as do 12% of the drivers themselves.⁵⁶

This issue is by no means clear-cut. Some transportation experts suggest that Mexican truckers actually do not want to roam the American southwest because they are not paid well enough to compensate for higher American fuel, food, and repair prices.⁵⁷ In addition, American manufacturers of large trucks see the dilapidation of the Mexican fleet as an opportunity to increase sales because in order to operate in the U.S., many Mexican trucking firms will have to upgrade their equipment.⁵⁸ Mexican truckers, like their American counterparts, are worried about competition. They fear the newer and more efficient American rigs, but perhaps unnecessarily so—American truckers may be reluctant to travel Mexico's rough roads, and the quality and consistency of diesel fuel in Mexico is different than it is in the U.S.⁵⁹ And, American truckers are not blameless, either—28% of American rigs fail the same cross-border safety test, as do 9% of American drivers.⁶⁰ As an issue of fact, then, cross-border trucking under NAFTA may be limited. Nevertheless, these concerns have led to temporary cutoff of access to the U.S. for Mexican truckers. The powerful Teamster's Union (which freely admits its anti-NAFTA effort was more about jobs than safety) has mounted an effective media and lobbying campaign to delay implementation of NAFTA's transportation provisions. The current stalemate over trucking access may ultimately jeopardize the entire pact.

Miscellaneous Objections

A variety of other objections are, properly or improperly, linked to the NAFTA treaty. Each year, approximately \$120 billion in illegal drugs move into the United States⁶¹ much of it through Mexico, generating by one estimate, twice the profit derived from the Mexican petroleum industry.⁶² "That's chemical warfare on our children . . ."

charges Ross Perot,⁶³ who likens NAFTA to “doing business with the enemy.” With intercepts of illegal drugs running at about 10% of total “imports”⁶⁴, however, it is difficult to see how withholding NAFTA from Mexico makes the problem better, or how it could get much worse. Consumer groups also opposed NAFTA because of its provisions for setting standards and resolving trade disputes. In essence, these groups fear foreign influence, particularly that of a foreign bureaucracy, over American citizens and their government.⁶⁵ However, Gary Hufbauer, visiting fellow at the Institute for International Economics, noted that such groups ignore the costs of tariffs (estimated to be \$53 billion in 1984) because they are hidden from easy view.⁶⁶ Even religion gets involved—Mexican Catholic bishops are on record as opposed to NAFTA, fearing that it would further concentrate wealth in the hands of the few in Mexico who have it and would not “trickle down” to impoverished Mexicans.⁶⁷

Illegal Immigration

As noted earlier, controlling illegal migration from Mexico was an unstated but important objective of the NAFTA treaty. Predictions for the effect of NAFTA on this problem vary widely, ranging from 260,000 to 1.1 million fewer illegal immigrants per year.⁶⁸ Opinions vary, too: in fact, one researcher suggests that NAFTA may actually be setting up a “system” which *encourages* more illegal immigrants to cross the border. Most new NAFTA development has taken place in the *maquiladora* zone—American firms are familiar with operations there and U.S. managers can easily live in the U.S. and commute to work across the border. Increasing employment opportunities in *maquiladora* zone will continue to attract Mexicans from the southern interior, but,

according to this theory, their ultimate goal will still be to live and work in the U.S. The zone, then, provides a staging area for attempts to slip across the border. The *maquiladora* will also provide immediate re-employment if the illegal is caught and returned to Mexico. Given more opportunities to try and a “safety net” in case of failure, illegal immigration may actually increase.⁶⁹ A few sources do not think that illegal immigration really is not a problem at all: that in fact, illegals are taking jobs that most Americans will not fill.⁷⁰ The *facts* are that apprehensions of illegal immigrants are up, from 979,000 in Fiscal Year 1994 to 1.27 million in FY 1995.⁷¹ Experts disagree about the cause of the increased apprehensions—there has been a border patrol crackdown along the border (coincident with the arrival of the presidential election cycle) and the Mexican economy is in severe recession (providing intense economic reasons for Mexicans to head north), but it is not definitively possible to blame or praise NAFTA for changes in illegal immigration numbers.⁷²

Politics

All of these concerns—job losses, environmental damage, health and safety, immigration—ultimately become political issues. As one supporter noted, the basic problem with NAFTA is not that the “benefits are . . . broad level [but the] costs . . . are painfully visible in laid-off workers and factory closures.”⁷³ That is, NAFTA is an easy target, but hard to defend. Sixty-seven percent of Americans are in favor of import tariffs in order to protect domestic jobs,⁷⁴ but few consider the benefits of free trade. The paradox was neatly put by Thomas Oliphant, who wrote that free trade was “. . . a controversial subject about which more Americans have no hard opinion. . . .”⁷⁵ There is

a growing popular feeling that the United States got “taken,” that NAFTA is just another “dumb trade pact,”⁷⁶ “an insider’s deal among transnational elites.”⁷⁷ This uneasiness about foreign competition in general and NAFTA in particular is reflected in the current campaign for President—Patrick Buchanan (whom one critic called a “pioneering xenophobe”⁷⁸) proposes not only abrogating NAFTA and building an electrified fence along the border (the so-called “Cactus Curtain”⁷⁹), but also withdrawing from the World Trade Organization and the Global Agreement on Trade and Tariffs (GATT).⁸⁰ Ross Perot (with Pat Choate) has even written a book about it (*Save Your Job, Save Our Nation*) which was described by critics as a “tirade” and something akin to a John Birch Society publication.⁸¹ “America Firsters” generate opposition with slogans like “First NAFTA, then SHAFTA.”⁸² Even onetime NAFTA cheerleader and Senate Majority Leader Bob Dole has backed away from the treaty, calling for a “cooling off” period before pursuing further trade negotiations.⁸³ It is probably correct to say that a “combustible mixture of economic nationalism and populism has re-emerged in American life. . . .”⁸⁴ Even in Mexico, the pact has become unpopular—two-thirds of those polled thought it was a threat to Mexican culture.⁸⁵

The growing opposition to NAFTA was further aggravated by the near-collapse of the Mexican economy. In its attempt to become first-world, the Mexican government went on a spending spree, investing heavily in capital and infrastructure projects, most of which required heavy levels of imported goods.⁸⁶ These improvements were funded by borrowing, and when the debt load got too high, the value of the peso plummeted. To make matters worse, the Mexican economy, superheated by the spending boom, began to suffer from inflation, and prices increased by 38% between December 1994 and August

1995.⁸⁷ With Mexicans unable to afford more imports from the United States, and Mexican products made cheaper by the decline of the peso, what had been a \$1.2 billion U.S. trade surplus with Mexico turned into a \$12 billion deficit.⁸⁸ In return for a Mexican austerity budget and increased opportunities for foreign investors to buy Mexican capital assets, President Clinton authorized \$18 billion in loan guarantees to Mexico.⁸⁹ Most experts applauded the President's unilateral actions to help Mexico: the Chief Executive Officer of CSX Corporation and Business Roundtable member John W. Snow, said that not approving the bailout would result in a "... drop in U.S. exports, increased illegal immigration, and [a] currency scare. . . ."⁹⁰ Others argued that NAFTA offered Mexico the opportunity to increase exports by exploiting the lower peso level (that is, offering Mexico the "chance to export its way out of trouble"⁹¹), and may have actually prevented the crisis from becoming much worse than it was.⁹²

Expert advice notwithstanding, the problems with the Mexican economy did substantial damage to NAFTA politically, and the "I told you so" argument moved to the become paramount. It offered opponents an opportunity to re-open the NAFTA debate, charging that the Clinton administration had supported an unstable and irresponsible government and "bailed out Wall Street" in the process.⁹³ Devaluation of the peso had a dramatic effect on Mexican wages in real terms—before the crisis, the average rate was \$2.54 per hour, but afterwards it had sunk to \$1.80.⁹⁴ *Black Enterprise* Magazine worried about the effect on blue-collar U.S. jobs: "If the peso remains dirt cheap, as it is now, the impact on U.S. jobs will be considerable. People at the bottom [i.e., blue collar workers, African-Americans, and other minorities] will see their jobs going south."⁹⁵ Some even

wondered if Mexico secretly wanted devaluation in order to increase its competitive edge, vis-à-vis the United States.⁹⁶

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Chapter 9

NAFTA: Success or Failure?

The preceding discussion is not, by itself, convincing proof that NAFTA has yet been a roaring success. A large increase in the trade deficit with Mexico, continuing environmental and safety problems, complaints about job losses, adverse impacts on some domestic industries, and seemingly unstoppable illegal immigration from Mexico would suggest otherwise. In addition, NAFTA has become politically damaged and may become an issue in the 1996 presidential election campaign. Even once-avid NAFTA supporter Senator Bob Dole, who chided then-Governor and presidential candidate Bill Clinton for wavering on the issue, has questioned the impact of the agreement, commenting that “. . . the verdict isn’t in yet . . .”¹ Or, is it?

Before deciding what you do not want to do, it is always useful to ask the question of the alternative—what else is there to do? For Americans who are losing their low-skill jobs to lower-paid Mexicans, there is no other outcome—those jobs were already in flight to Asia and other distant underdeveloped nations where the employment and prosperity they create does nothing to enhance U.S. national security. The industrial reality of today’s American is that many firms, particularly low-tech and low-skill ones, *are* moving overseas. Looking at the long term result, moving to Mexico, may actually be good—one study of firms which had moved to the *maquiladora* zone reported initial job losses in

low-skill trades, but ultimately, for each job lost, posted another one or two job gains in transportation, management, distribution, and engineering.² According to the Federal Reserve Bank of Dallas, in a non-NAFTA world (the Perot/Buchanan alternative), these Mexican-based businesses would probably have moved to the Asian economic dynamo.³ NAFTA, however, provides businesses a low-tariff incentive to stay in North America and a way to effectively compete with Asia.⁴ The proximity of Mexico also offers American firms the opportunity domestically to manufacture components for follow-on assembly in Mexico. The distance to Asian factories, however, is a severe disadvantage for potential U.S. parts suppliers.⁵ For the environmentalists, the alternative is the *status quo*—more pollution in the Rio Grande, more smog in south Texas, more raw sewage on southern California beaches. Progress on these fronts “. . . depends first on a healthy dose of prosperity. . . .”⁶ For those concerned about Mexican working conditions, the alternative is the conditions created by Mexican unemployment—homelessness, hunger, and ultimately, political discontent. For those worried about illegal immigration (as all Americans should be), any incentive (that is, the jobs created by NAFTA) for Mexicans to stay in Mexico is better than widespread unemployment, which is an outright encouragement to cross the border. And, for those concerned about America’s status as a trading nation should look with some alarm at the alternative which is now playing out in South America—discouraged by the lack of progress in extending NAFTA to Chile and other nations (as proposed by President Clinton at the “Summit of the Americas” in 1994⁷) and beyond, South American governments are forming their own trade pacts, actively courting European firms, and discussing pacts with the European Union, *to the exclusion of the United States*.⁸

Here is a simple fact: "... outrage at the status quo can't change it."⁹ NAFTA critics are unhappy with the way things are, but offer no reasonable alternatives which can improve it. These skeptics are apparently willing to endure the worsening disadvantages of "the way things are." But, the alternative NAFTA offers is not zero sum: "... a thriving Mexico would help America, and an impoverished America would hurt [America]."¹⁰

A bigger stake in the current debate is what NAFTA does for American world leadership. NAFTA "... resolves America's post-cold war identity crisis."¹¹ The United States can only pursue its policy of "engagement and enlargement" if it is *not* entrenched behind trade and tariff barriers. Alternatively, a retreat from NAFTA would signal America's diminished interest in world leadership. NAFTA also has powerful implications for breaking down trade barriers elsewhere: for example, how can we insist on "free trade" and a "level playing field" with the Japanese while we deny "free trade" and a "level playing field" to our next-door neighbor? Finally, without NAFTA, how will we be able to tilt the balance of power in the Pacific back towards its American rim?

What effect will the alternative (that is, no NAFTA) have on American national security? One of the historic hallmarks of this nation's security—the Monroe Doctrine—was really a very simple idea: the Western Hemisphere is "our" zone of influence and we do not let threats to the United States develop in it. But there are two threats currently developing in our "Monroe Doctrine zone." One is the Mexican time bomb, where poverty and population growth may result in political chaos, a deluge of refugees, and potentially, a government increasingly frustrated by exclusion, and growing hostile to the United States. The other is the growing influence of European and Asian trading partners

in South America, *to the exclusion of the United States*. NAFTA, in its present, imperfect form is the only tool we have to address the first problem. And, NAFTA, as it was intended to be [that is, extended to Chile and the rest of Latin America], is our only option for preserving America's hemisphere-wide influence: that is, preserving our Monroe Doctrine zone.

It is a lopsided choice—the United States is currently paying a price for including Mexico in the NAFTA. Jobs have been lost, industries relocated, a trade surplus has become a trade deficit. And, worst of all, the domestic political pot has been vigorously stirred. But, the United States has more problems south of its southern border than the price it is currently paying for NAFTA—on a long-term, cost/benefit basis, NAFTA may be the best national security bargain around.

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